F.A.C.

ANNUAL REPORT

1966

FRONTIER ACCEPTANCE CORPORATION LIMITED

ANNUAL REPORT

FOR THE YEAR ENDED MARCH 31, 1966

F.A.C.

Frontier Acceptance Corporation Limited

DIRECTORS:	JOHN W. ADAMS BENTLEY I. BALDWIN C. NORMAN CHAPMAN MURRAY J. HOWE CHARLES E. ISARD PETER J. IVEY LYMAN W. OEHRING, JR. FRANK T. SHERK
OFFICERS:	LYMAN W. OEHRING, JR. — President C. NORMAN CHAPMAN — Vice-President HOWARD L. KIRBY — Vice-President JOHN A. PARK — Vice-President ROBERT W. STEVENS — Secretary PETER J. IVEY — Assistant Secretary
LEGAL COUNSEL:	BLAKE, CASSELS & GRAYDON, Toronto, Ontario
AUDITORS:	PEAT, MARWICK, MITCHELL & CO., Toronto, Ontario
BANKERS:	BANK OF MONTREAL, Toronto, Ontario THE ROYAL BANK OF CANADA, Toronto, Ontario
TRANSFER AGENT:	THE ROYAL TRUST COMPANY, Toronto, Ontario
SECURITIES LISTED:	TORONTO STOCK EXCHANGE 6½% cumulative redeemable convertible first preference shares Series A Common shares
TRUSTEE:	MONTREAL TRUST COMPANY, Toronto, Ontario 6¾% Subordinated Sinking Fund Debentures Series A
HEAD OFFICE:	5385 YONGE STREET, Willowdale (Metropolitan Toronto), Ontario
BRANCHES:	5385 YONGE STREET, Willowdale, Ontario 380 ST. GEORGE STREET, Moncton, New Brunswick 110 PLACE CREMAZIE WEST, Montreal, Quebec

May 9, 1966

TO OUR SHAREHOLDERS:

During the past year the finance industry has been beset with many difficulties and much unfavourable publicity. Criticism has been levelled at it by the public, both as investors and as borrowers, by institutional investors and investment bankers, and by various levels of government. The resulting loss of confidence in the industry, coupled with an overall tightening in the money markets, has reduced the availability of and increased the cost of money to finance companies.

Although on the surface certain events of the past year may have justified some concern about the industry, a closer analysis over a period of time has proved that any cause for serious concern was limited to a few specific companies. Most finance companies reacted to the changing conditions in a most responsible way and are continuing to operate in an efficient manner. Since its beginning, the finance industry has performed well, both in service to the public and in profitability to its investors and lenders. Other industries have suffered more casualties during their lifetimes but with much less pubilicity. Ours, however, since it is dealing in money and credit, affects a broad segment of the community.

The services financing agencies provide are indispensable in our present day society. The people of North America, primarily because of mass production, enjoy the highest level of material wealth and consumption in the world. Mass production can only exist in partnership with mass consumption. Financing agencies have provided the means for consumers to purchase durable goods on a volume basis. Although time sales financing was originally initiated to help satisfy the demand for automobiles, the finance industry has had the flexibility to develop programs enabling the consumer to finance the purchase of a broad range of items. In effect the finance industry has been the catalyst in the combining of our mass production capability with our mass consumption appetite. Just consider what would happen to our factories and the jobs they provide if there was no consumer credit and all automobiles, mobile homes, appliances, and other things which have become necessities in our modern life could only be sold for cash.

In spite of this record of service, many proposals are being put forward with a view to further restricting and controlling finance companies, both as borrowers and as lenders. Additional proposals may develop from the governmental inquiries now in process. Some of them may have merit, but some have been hastily contrived without due consideration for their future consequences. Competition among members of the finance industry has kept, and will continue to keep, consumer borrowing costs at a minimum consistent with costs of money and operating expenses. Legal restrictions, such as abolishing wage assignments, involved calculations of effective rates of interest, limitations on rights of repossession and foreclosure, and putting product responsibility on financial organizations who have no control over the product will increase the costs of operations of both the sellers of goods and the organizations that finance the sales. These measures, proposed ostensibly to "protect" the consumer, will only shield the small percentage of persons who, through lack of understanding and improper planning, misuse and abuse the credit available to them. The overall effect of increasing costs of business will reduce flexibility, and will increase costs and reduce availability of credit to all consumers. These inescapable consequences of increased costs, at this time due primarily to the higher money costs previously discussed, are already evidencing themselves at the consumer level.

Much more lasting good could be accomplished by educating and counselling people, especially young people in school, as to the proper uses of credit.

One sound development is the pressure for more detailed disclosure of the operations of all companies. We believe this to be very constructive and healthy. The investors in and lenders to a company in any industry should know what that company is doing. Recent annual reports of finance companies contain a great deal more information and statistical data, and are indicative of how rapidly our industry can respond to proper changes without the necessity of restrictive legislation.

In this annual report you will find detailed disclosures and comments about your company's business. We have tried to make them understandable, clear and concise, and we believe they are complete enough to enable an investor or a lender to satisfy himself as to the Company's policies and the actual results experienced in applying these policies. We welcome any suggestions from our shareholders and the investment community as to improvements for the future.

The past year has been a good one for Frontier. In spite of the reduced availability of new funds we experienced a 25% increase in outstanding receivables. A major subordinated debt financing was completed with a large U.S. institution. Net earnings increased almost 27%. We have experienced a growth in outstanding receivables and net earnings each year since the Company was founded in 1958. A new branch was opened in Montreal and we can now physically serve a large part of the population of the eastern half of Canada. Our overall organization has been strengthened and improved. The quality and profitability of our receivables and the effectiveness and efficiency of our staff are being subjected to ever increasing scrutiny.

Although our growth this past year could have been greater if more funds had been available, we are proud of the results we achieved, many of which do not show in this year's financial statements but will evidence themselves in future years. We are optimistic about the future of the finance industry and about our ability to grow with it. Changes in the money markets will always be with us and will always affect us. Their consequences, however, will be felt more in the short run, and we have every confidence in the long-term future.

It is customary here to thank the people who have made the results of the past year possible, and this we most heartily do. The loyalty of our employees and customers has been, and will always be, indispensable. A separate comment is due our two bankers, Bank of Montreal and The Royal Bank of Canada. Their outstanding loyalty and constructive advice and counsel during this past year while they were under extreme pressure themselves deserve a very special "thank you".

On behalf of the Board of Directors

President

REVIEW OF OPERATIONS

RECEIVABLES

Again this year, as in each year since the Company's founding in 1958, outstanding receivables are at an all time high with retail notes receivable 23.10% above the retail notes receivable of a year ago. The following is a breakdown of the outstanding retail notes receivable at March 31, 1966 and March 31, 1965 by type of business, and also the average amount per outstanding account in each category.

	MARCH 31, 1966			MARCH 31, 1965		
	Amount	Per Cent of Total	Average Amount Per Account	Amount	Per Cent of Total	Average Amount Per Account
Mobile homes	$ 4,454,043	40.29%	$4,820	$3,314,451	36.91%	$4,662
Direct cash loans	3,282,844	29.70	4,114	2,625,721	29.24	4,263
Automobiles	817,489	7.39	1,658	563,541	6.28	1,991
Home improvements	678,841	6.14	545	599,069	6.67	782
Appliances	326,708	2.96	257	653,288	7.27	342
Equipment leases	349,735	3.17	1,249	140,214	1.56	719
Commercial loans	1,144,176	10.35	7,891	1,083,598	12.07	3,070
Total	$11,053,836	100.00%	$2,142	$8,979,882	100.00%	$1,854

Almost all of the Company's retail notes receivable include precomputed interest to the maturity of the loan. This increases the average amount per account to an amount greater than the Company's actual investment.

Wholesale notes receivable at March 31, 1966 and March 31, 1965 were $1,282,725 and $903,540, respectively, and consist primarily of mobile homes held for sale by dealers who customarily sell their retail notes receivable to the Company.

The branch office in Willowdale, Ontario, handles all types of business. Presently, the branch office in Moncton, New Brunswick, and the new branch office in Montreal, Quebec, engage only in sales financing in the Maritimes and Quebec. At March 31, 1966 the Moncton and Montreal offices were servicing retail notes receivable of $1,670,000 and $1,552,000, respectively, consisting almost entirely of mobile homes.

The Company is developing a diversified portfolio covering the three major areas of normal finance company activities; sales financing, direct cash loans, and commercial loans of various types. In determining areas of financing in which to engage, emphasis is placed on quality and overall profitability rather than on volume and size alone.

All classes of loans are made only on a secured basis. The sales finance contracts are basically secured by the item the customer is purchasing, such as a mobile home, automobile, appliance, etc. In addition, a large percentage of this business is purchased with recourse to the dealer, with the dealers' contingent obligations being further supported by dealers' reserves. The majority of the direct cash loans are not only secured by chattel mortgages on personal property, but also by second mortgages on real estate. Equipment leases are secured by assignments of the leases and liens on the leased equipment. Commercial loans are secured by liens on real or personal property, by assignments of accounts and notes receivable, or by a combination thereof.

Except for mobile home contracts which, because they are for homes with correspondingly larger amounts involved, have a maximum maturity of seven years, almost all of the credit the Company extends is for five years or less. Direct cash loans with an original maturity of over three years are normally secured by real estate mortgages.

Generally, the Company restricts total loans to any one customer to $25,000 or less. All large loans and all loans of an unusual nature are subjected to an extensive review by senior management prior to approval, and to special follow-up activity during the life of the loan. No loans are made to officers or Directors, or to their families, associates, or affiliates.

Volume of purchases of retail instalment notes during the past year totalled $8,407,939. The following schedule details these purchases by type of receivable and original maturity.

ORIGINAL MATURITY OF NOTES
(IN THOUSANDS OF DOLLARS)

	Two Years and Under	Two to Three Years	Three to Four Years	Four to Five Years	Five to Six Years	Six to Seven Years	Total	Per Cent of Total
Mobile homes	$ 121	$ 162	$218	$ 322	$229	$1,774	$2,826	33.61%
Direct cash loans	47	386	55	1,793	8		2,289	27.23
Automobiles	281	575	3				859	10.21
Home improvements	2	7		333			342	4.07
Appliances	59	113					172	2.04
Equipment leases	8	36	38	268			350	4.16
Commercial loans	1,234	107	44	136	49		1,570	18.68
TOTAL	$1,752	$1,386	$358	$2,852	$286	$1,774	$8,408	100.00%
Per Cent of Total	20.84%	16.48%	4.26%	33.91%	3.41%	21.10%	100.00%	

Scheduled future liquidations of the Company's retail notes receivable outstanding at March 31, 1966 are as follows.

Scheduled liquidation during the year ending March 31:	Amount	Per Cent of Total
1967	$ 3,719,851	33.65%
1968	2,623,101	23.72
1969	1,898,689	17.18
1970	1,372,135	12.41
1971	905,887	8.20
1972	373,248	3.38
Subsequent to March 31, 1972	160,925	1.46
TOTAL	$11,053,836	100.00%

Based on scheduled collections it would take 16 months' collections to repay the Company's short-term secured debt, after first deducting therefrom cash and wholesale notes receivable.

DELINQUENCIES AND LOSSES

The total unpaid balance of retail notes receivable outstanding at March 31, 1966 and March 31, 1965 with payments more than 60 days past due were as follows.

	MARCH 31, 1966		MARCH 31, 1965	
	Outstanding Amount	Per Cent to Total Retail	Outstanding Amount	Per Cent to Total Retail
Total unpaid balance of accounts with payments:				
61 to 90 days past due	$ 77,609	.70%	$120,265	1.34%
Over 90 days past due	151,506	1.37	197,928	2.20
Total over 60 days past due	$229,115	2.07%	$318,193	3.54%

The improvement since a year ago reflects the increased emphasis on an efficient collection operation and more selective credit judgments in all areas of the business. Included in the above accounts over 90 days delinquent were $67,366 at March 31, 1966 and $112,919 at March 31, 1965 representing accounts on which the Company has been forced to institute legal action but has not yet started receiving payments as a result of such legal action. This improvement again reflects a more positive collection follow-up.

As was expected, the faster and more intensive collection activity, especially over the winter months, resulted in a slight increase in repossessions on hand. At March 31, 1966 repossessions totalled $171,624 as compared with $126,380 at March 31, 1965. Again, these balances include interest to maturity which means the Company's investment is a lesser amount. Of the repossessions on hand at March 31, 1966, $116,602 is due from dealers under recourse and repurchase agreements. The dealers involved are all in business and active with the Company, and the Company holds substantial dealer reserves in relation to the unpaid repossessions. The summer months provide a better selling season and the Company does not expect any significant losses from the liquidation of repossessions.

In order to properly liquidate accounts, it is sometimes necessary to alter the repayment terms of certain loans, primarily due to changed economic conditions on the part of the customer after the loan is made. These changes are a vital part of the finance business and can furnish additional income in the form of extra fees. The practice can be subject to abuse, however, and it is the Company's policy to grant such changes in terms only for good cause and only when the customer demonstrates a definite desire to maintain a good payment record.

The Company has continued its policy of charging off accounts which appeared doubtful of collection. Retail liquidations and losses for the past two years and since inception of the Company are as follows.

	Retail Liquidations	Retail Losses	Per Cent Losses to Liquidations
Year ended March 31:			
1966	$ 6,333,985	$ 90,162	1.42%
1965	5,357,590	85,379	1.59
Total May 1, 1958 (inception) to March 31, 1966	18,524,913	204,787	1.11

Along with the increased collection emphasis on regular and litigation accounts, increased attention was given to recoveries on accounts previously written off. Retail losses for the year ended March 31, 1966 are shown net of recoveries of $11,774 (11.55% of gross charge offs) on previously written off accounts. The faster follow-up procedures now in effect should result in more recoveries in the future.

Losses first evidence themselves as delinquent accounts, and it is the Company's opinion that the marked decrease during the past year in the percentage of accounts over 60 days delinquent is an indication that continued improvement in the percentage of losses to liquidations can be expected in the future.

Based on experience to date the allowance for possible losses at March 31, 1966 of $121,443, which is 1.09% of outstanding retail notes receivable, is considered adequate to absorb any losses which may be incurred in the collection of the present receivables. Dealers' credit balances of $313,690 at March 31, 1966 (2.84% of outstanding retail notes receivable) are also available to reduce future credit losses on retail accounts which were purchased with recourse to the dealer.

ACCOUNTING POLICIES

The Company grants credit on two different bases. In a small percentage of cases the loans are made on an interest-bearing basis, i.e. the interest is computed and billed to the customer monthly based on money in use. On this type of loan income is recorded on a monthly basis as it is earned.

In most cases the charges for the life of the contract are precomputed and included in the face of the note. The difference between the amounts advanced by the Company and the total amounts to be repaid by the customers is recorded as unearned finance charges. The Company does not record any earnings in the month a contract is acquired as representing an "acquisition cost", but takes the finance charges into income over the terms of the respective notes based on the declining amounts outstanding. Mechanically, this is accomplished by applying the sum-of-the-digits (sometimes referred to as the "rule of 78's") amortization method to the finance charges.

This overall policy results in the realization of no income at the time a contract is purchased and has resulted in a very substantial unearned finance charge account in relation to outstanding retail notes receivable with precomputed interest, as is shown below.

	March 31, 1966	March 31, 1965
Total retail notes receivable	$11,053,836	$ 8,979,882
Less interest bearing notes receivable	452,571	332,025
Retail notes receivable with precomputed interest	$10,601,265	$ 8,647,857
Unearned finance charges	$ 1,848,510	$ 1,440,102
Percentage of unearned finance charges to notes receivable with precomputed interest	17.44%	16.65%

These unearned finance charges represent future gross income and will be recorded as earnings over the remaining terms of the outstanding notes receivable.

All expenses are charged immediately to income as they are incurred except for normal deferred items such as prepaid interest, insurance and taxes, and any discounts and expenses in connection with long-term debt issues which are charged to earnings over the terms of the respective debt issues involved.

FINANCING

In December, 1965 the Company placed privately with a large institutional purchaser an issue of 6⅞% Senior Subordinated Notes due December 15, 1977, in the amount of $2,000,000 (U.S.). This placement increased the total capital funds (sum of shareholders' equity and subordinated debt) to over $4,000,000 and should enable the Company to substantially increase its senior debt, and thereby its outstanding notes receivable, before any additional capital or subordinated debt is required. The following table shows the composition of the Company's debt and capital structure at March 31, 1966 and at March 31, 1965.

	MARCH 31	
	1966	1965
Secured indebtedness to banks	$ 5,873,000	$ 5,941,623
Capital funds:		
Subordinated debt	$ 3,054,250	$ 1,000,000
Shareholders' equity:		
Preference	$ 384,250	$ 475,000
Common	842,881	652,768
Total shareholders' equity	$ 1,227,131	$ 1,127,768
Total capital funds	$ 4,281,381	$ 2,127,768
Total debt and capital	$10,154,381	$ 8,069,391

The Company's only short-term indebtedness is to its two banks under established lines of credit, and the Company does not intend to borrow any funds in the short-term market except from banks or unless such borrowings are fully covered by unused bank lines of credit.

The decrease in preference shares during the year resulted primarily from conversion into common shares. The conversion price on the Company's first preference shares Series A increased effective November 1, 1965, and in October 3,230 first preference shares Series A were converted into 16,150 common shares. In addition the Company repurchased 400 first preference shares Series A out of a purchase fund provided for that purpose.

EARNINGS

Net earnings for the year ended March 31, 1966 were $138,925, an increase of 26.77% over net earnings of $109,592 for the year ended March 31, 1965. The distribution of gross income for the last two years is as follows.

	YEAR ENDED MARCH 31			
	1966		1965	
	Amount	Per Cent of Gross Income	Amount	Per Cent of Gross Income
GROSS INCOME	$1,205,892	100.00%	$900,129	100.00%
COSTS AND EXPENSES:				
Cost of borrowings	$ 523,287	43.39%	$350,837	38.98%
Salaries and wages	144,229	11.96	102,124	11.34
Other general and administrative expenses	157,504	13.06	123,569	13.73
Provision for possible losses	112,947	9.37	110,788	12.31
Taxes on income	129,000	10.70	103,219	11.47
NET EARNINGS	$ 138,925	11.52%	$109,592	12.17%

As can be seen the major change is in the increased percentage of gross income going towards the cost of money. This has been caused by the increased use of borrowed funds in relation to capital and the general overall increase in interest rates. To offset the higher money costs now being experienced, lending rates have been moderately increased wherever possible. This has a delayed effect on earnings, however, since rates cannot be increased on loans previously made.

Operating expenses are more controllable and have increased at approximately the same rate as the increase in business. These expenses are continually under review and every effort is made to keep them at a minimum consistent with a sound business operation.

In spite of the aforementioned increase in earnings and the increase in earnings for common shareholders from $77,092 last year to $109,538 for the year just ended, earnings per common share remained approximately the same. For the year ended March 31, 1966 they were $.61 a share as compared with $.60 a share for the year ended March 31, 1965. This was due to an increase in the average number of common shares outstanding from 128,729 to 179,208.

During the past two years there has been quite an increase in equity and outstanding shares in order to support an expanding level of receivables. Under normal circumstances additional increases will not be necessary in the immediate future. This will mean that any earnings increases in the near future will also be reflected as corresponding increases in earnings per common share.

FRONTIER ACCEPTANCE CORPORATION LIMITED
AND ITS WHOLLY-OWNED SUBSIDIARIES

Consolidated Balance Sheet — March 31, 1966
(with comparative figures for March 31, 1965)

ASSETS

	1966	1965
Cash	$ 86,554	$ 2,065
Notes receivable:		
Retail (Note 1)	$11,053,836	$ 8,979,882
Wholesale	1,282,725	903,540
	$12,336,561	$ 9,883,422
Less:		
Unearned finance charges	$ 1,848,510	$ 1,440,102
Allowance for possible losses	121,443	98,658
	$ 1,969,953	$ 1,538,760
NOTES RECEIVABLE — NET	$10,366,608	$ 8,344,662
Accounts receivable	29,307	28,718
Prepaid expenses	9,290	5,308
Furniture, equipment and leasehold improvements — at cost	$ 30,359	$ 23,371
Less accumulated depreciation and amortization	13,285	10,008
	$ 17,074	$ 13,363
Unamortized debt discount and expense (Note 2)	159,298	31,451
	$10,668,131	$ 8,425,567

Approved on behalf of the Board:

L. W. OEHRING, JR., Director.

J. W. ADAMS, Director.

LIABILITIES AND SHAREHOLDERS' EQUITY

		1966	1965
Short-term notes payable to banks — secured by assignment of certain notes receivable:			
Overdraft			$ 130,623
Loans		$ 5,873,000	5,811,000
		$ 5,873,000	$ 5,941,623
Accounts payable and accrued liabilities		134,936	85,261
Income and other taxes payable		65,124	19,929
Dealers' credit balances		313,690	250,986
Capital funds:			
Subordinated debt (Note 3):			
6⅞% Senior Subordinated Notes		[illegible]	
6¾% Subordinated Sinking Fund Debentures Series A		903,000	$ 1,000,000
TOTAL SUBORDINATED DEBT		$ 3,054,250	$ 1,000,000
Shareholders' equity:			
Capital stock (Note 4):			
Authorized:			
35,370 first preference shares with a par value of $25 each, issuable in series	$884,250		
1,000,000 common shares without par value	—		
Issued:			
15,370 6½% cumulative redeemable convertible first preference shares Series A, with a par value of $25 each		$ 384,250	$ 475,000
188,685 common shares — stated value		512,963	431,988
		$ 897,213	$ 906,988
Retained earnings (Note 5)		329,918	210,780
Purchase fund — in respect of 6½% cumulative redeemable convertible first preference shares Series A			10,000
TOTAL SHAREHOLDERS' EQUITY		$ 1,227,131	$ 1,127,768
TOTAL CAPITAL FUNDS		$ 4,281,381	$ 2,127,768
		$10,668,131	$ 8,425,567

See accompanying Notes to Financial Statements

FRONTIER ACCEPTANCE CORPORATION LIMITED

AND ITS WHOLLY-OWNED SUBSIDIARIES

Consolidated Statement of Earnings and Retained Earnings
Year Ended March 31, 1966

(with comparative figures for the year ended March 31, 1965)

	1966	1965
Income — finance charges, interest and fees earned	$ 1,205,892	$ 900,129
Deduct:		
Salaries and wages	$ 144,229	$ 102,124
Other general and administrative expenses (Note 6)	157,504	123,569
Provision for possible losses	112,947	110,788
	$ 414,680	$ 336,481
EARNINGS BEFORE COST OF BORROWINGS AND TAXES ON INCOME	$ 791,212	$ 563,648
Cost of borrowings, principally interest	523,287	350,837
EARNINGS BEFORE TAXES ON INCOME	$ 267,925	$ 212,811
Taxes on income	129,000	103,219
NET EARNINGS	$ 138,925	$ 109,592
Retained earnings at beginning of year	210,780	164,710
Income tax credit on exchange loss arising from retirement of 6¾% subordinated notes		13,601
	$ 349,705	$ 287,903
Deduct:		
Dividends on 6½% cumulative redeemable convertible first preference shares Series A	$ 29,387	$ 32,500
Transfer to (from) purchase fund, 6½% cumulative redeemable convertible first preference shares Series A	(10,000)	10,000
Premium paid on the redemption of 400 6½% cumulative redeemable convertible first preference shares Series A	400	
Underwriters' commission and other expenses in connection with the issue of common shares		32,281
Excess of cost of shares of subsidiary company over underlying assets		1,717
Foreign exchange loss on retirement of 6¾% subordinated notes		625
	$ 19,787	$ 77,123
Retained earnings at end of year	$ 329,918	$ 210,780

See accompanying Notes to Financial Statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
Year Ended March 31, 1966

NOTE 1 — Retail Notes Receivable

Of the retail notes receivable outstanding at March 31, 1966, instalments aggregating $3,719,851 are due within one year.

NOTE 2 — Unamortized Debt Discount and Expense

Unamortized debt discount and expense is shown net of accumulated tax reductions of $38,178 and accumulated amortization of $18,264.

NOTE 3 — Subordinated Debt

The 6⅞% Senior Subordinated Notes are payable, both as to principal and interest, in U.S. funds. The Notes are for $2,000,000 (U.S.) and are shown at the rate of exchange on December 16, 1965, the date of issuance. The Notes are due December 15, 1977 and the Company has covenanted to establish a sinking fund to provide for the retirement of $200,000 (U.S.) principal amount of the Notes on December 15, in each of the years 1968 to 1976, both inclusive. The Notes are presently redeemable, otherwise than out of sinking fund monies, in whole or in part at a premium of 5% of such principal amount if redeemed on or before December 15, 1966 with the premium thereafter decreasing rateably each year to zero if redeemed after December 16, 1976.

The 6¾% Subordinated Sinking Fund Debentures Series A are due June 15, 1979. The Company has covenanted to establish a sinking fund to provide for the retirement of $50,000 principal amount of the Debentures on June 15, in each of the years 1965 to 1974, both inclusive, and $100,000 principal amount of the Debentures on June 15, in each of the years 1975 to 1978, both inclusive. The Debentures are presently redeemable, otherwise than out of sinking fund monies, in whole or in part at a premium of 4.625% of such principal amount if redeemed on or before June 15, 1966 with the premium thereafter decreasing rateably each year to zero if redeemed after June 15, 1978.

NOTE 4 — Capital Stock

The 6½% cumulative redeemable convertible first preference shares Series A are convertible, on or before October 31, 1970, into common shares at the rate of 4 common shares for each first preference share Series A on or before October 31, 1967 and thereafter at a declining rate. The first preference shares Series A are redeemable at a price of $26.00 a share. During the year ended March 31, 1966, 3,230 first preference shares Series A were converted into common shares and 400 first preference shares Series A were redeemed by the Company out of a purchase fund provided therefor at a price of $26.00 a share. The Company is required to enter on its books to the credit of a purchase fund certain amounts to be used for the purchase of first preference shares Series A, which obligation can be anticipated by the redemption or conversion of first preference shares Series A. At March 31, 1966 no amounts were required to be set aside for such purchase fund.

Of the authorized and unissued common shares, 61,480 shares are reserved for conversion of the first preference shares Series A; 14,865 shares are reserved for share purchase warrants (issued in connection with the 6¾% Subordinated Sinking Fund Debentures Series A) exercisable at $8.50 a share on or before June 15, 1967 and increasing to $12.50 per share on or before expiration date June 15, 1970; 40,000 shares are reserved for share purchase warrants (issued in connection with the 6⅞% Senior Subordinated Notes) exercisable at $6.25 a share on or before expiration date December 15, 1977; and 14,900 shares are reserved for executive stock options (issued to three officers) exercisable at $7.50 a share. One option is for 10,000 shares exercisable at the rate of 2,000 shares per year and expires on February 28, 1975; one option is for 3,500 shares exercisable at the rate of 500 shares per year and expires on September 14, 1971; and one option is for 1,400 shares exercisable at the rate of 200 shares a year and expires on June 30, 1972. All options may be exercised on a cumulative basis. During the year 16,150 common shares were issued upon conversion of first preference shares Series A and 30 common shares were issued at $7.50 a share upon exercise of share purchase warrants.

NOTE 5 — Retained Earnings

The Company's various loan agreements and its Letters Patent relating to the first preference shares Series A contain provisions relating to the payment of dividends on common shares. Under the most restrictive of these provisions no amount of retained earnings was available at March 31, 1966 for the payment of dividends on common shares.

NOTE 6 — Directors' Fees and Depreciation and Amortization

Other general and administrative expenses includes directors' fees for services as such of $3,010 (1965 — $2,317) and depreciation and amortization of $4,530 (1965 — $4,658).

AUDITORS' REPORT

TO THE SHAREHOLDERS,
FRONTIER ACCEPTANCE CORPORATION LIMITED.

We have examined the consolidated balance sheet of Frontier Acceptance Corporation Limited and its wholly-owned subsidiaries as of March 31, 1966 and the consolidated statement of earnings and retained earnings for the year ended on that date. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated balance sheet and consolidated statement of earnings and retained earnings present fairly the financial position of the companies at March 31, 1966 and the results of their operations for the year ended on that date, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

TORONTO, ONTARIO,
MAY 9, 1966.

PEAT, MARWICK, MITCHELL & CO.,
Chartered Accountants.

FRONTIER ACCEPTANCE CORPORATION LIMITED
AND ITS WHOLLY-OWNED SUBSIDIARIES

EIGHT YEAR SUMMARY

	1966
Operating results for the year:	
Finance charges, interest and fees earned	$ 1,205,892
Salaries and wages	144,229
Other general and administrative expenses	157,504
Provision for possible losses	112,947
Cost of borrowings	523,287
Times cost of borrowings earned	1.51
Taxes on income	129,000
Net earnings	138,925
Preference dividends	29,387
Times preference dividends earned	4.73
Net earnings for common shares	109,538
Net earnings per common share based on average shares outstanding	.61
Financial position at the end of the year:	
Notes receivable:	
Retail	$11,053,836
Wholesale	1,282,725
TOTAL NOTES RECEIVABLE	12,336,561
Unearned finance charges	1,848,510
Percent to retail notes receivable with precomputed interest	17.44%
Allowance for possible losses	121,443
Percent to retail notes receivable	1.09%
Short-term notes payable to banks — secured	5,873,000
Capital funds:	
Subordinated debt	3,054,250
Shareholders' equity:	
Preference stock	384,250
Common shareholders' equity	842,881
TOTAL SHAREHOLDERS' EQUITY	1,227,131
TOTAL CAPITAL FUNDS	4,281,381
Number of common shares outstanding	188,685
Book value per common share	4.47

1965	1964	1963	1962	1961	1960	1959
$ 900,129	$ 601,789	$ 449,550	$ 173,323	$ 93,678	$ 66,667	$ 15,011
102,124	73,624	44,563	27,226	13,440	11,256	7,400
123,569	91,352	76,084	42,018	15,168	11,433	12,357
110,788	59,372	37,550	4,491	1,082		
350,837	212,602	158,764	48,513	32,723	22,037	3,500
1.61	1.78	1.84	2.05	1.96	2.00	
103,219	73,900	57,800	8,054	8,575	3,200	
109,592	90,939	74,789	43,021	22,690	18,741	(8,246)
32,500	8,200					
3.37	11.90					
77,092	82,739	74,789	43,021	22,690	18,741	(8,246)
.60	.70	.64	.37	.38	.31	(.14)
$8,979,882	$5,978,292	$4,100,704	$2,174,619	$ 779,526	$ 699,584	$ 223,754
903,540	534,284	305,886	149,582			
9,883,422	6,512,576	4,406,590	2,324,201	779,526	699,584	223,754
1,440,102	969,187	746,216	399,914	93,000	90,516	25,839
16.65%	16.21%	18.20%	18.39%	11.93%	12.94%	11.55%
98,658	73,249	30,088	12,917	1,086		
1.10%	1.23%	.73%	.59%	.14%		
5,941,623	3,968,768	2,530,951	1,258,250	602,822	558,139	175,162
1,000,000	540,000	637,500	420,000			
475,000	500,000	28,800	28,800	28,800	28,800	28,800
652,768	195,910	159,164	94,344	34,385	11,695	(7,046)
1,127,768	695,910	187,964	123,144	63,185	40,495	21,754
2,127,768	1,235,910	825,464	543,144	63,185	40,495	21,754
172,505	117,400	117,400	117,400	60,000	60,000	60,000
3.78	1.67	1.36	.80	.57	.19	

corp report

SEMI-ANNUAL REPORT

SEPTEMBER 30

1966

file

FRONTIER ACCEPTANCE CORPORATION LIMITED

November 7, 1966

TO OUR SHAREHOLDERS:

Net earnings for the six months ended September 30, 1966 were $63,871 as compared with $62,307 for the six months ended September 30, 1965. Earnings per common share after preference dividends were $.27 and $.26, respectively, for the two six month periods.

We are sorry to have to report to you that we have not been successful in arranging any new financing since the end of our last fiscal year. We were hopeful that the substantial increase in our capital base last year along with respectable earnings, delinquencies and losses would make it possible for us to continue to expand our borrowings and thereby our outstanding receivables. However, the continued tightness of the money markets along with the stigma still attaching to small and medium sized finance companies has made it impossible up to now to interest any new institutional lender, either in Canada or the United States, in Frontier. This has been further aggravated recently by problems experienced by additional finance companies and by the very high rates of interest being offered by some of the largest finance and industrial companies. A note on the brighter side is the very fine relationship we have with our existing lenders. We keep them closely advised of current developments concerning the Company, and to date they appear to be completely satisfied with the way in which we are conducting our business.

We have not by any means become discouraged, but it behooves us as management to be realistic. We intend to continue our search for additional funds, but in the meantime we have been aiming at maximizing profits on our existing resources. We have been able to make our receivables more productive by selectively increasing rates where conditions warrant and by reinvesting repayments on existing loans into higher yielding types of receivables. In this connection we have been able to significantly reduce our wholesale receivables which, since they are an accommodation for our dealers who provide us with retail receivables, carry a relatively low rate of interest.

In addition to increasing our gross income, we are attempting, wherever possible, to control expenses. Our cost of borrowings is taking a larger percentage of our income, but there is not much we can do about this item at this time. Other expenses required to service a larger portfolio of receivables have also increased. It may be possible to reduce them somewhat, but we have purposely not cut them to the bone. Our ability to raise funds when they do become available will be directly affected much more by the quality and performance of our receivables than by large increases in earnings. It should also be noted that in the long run sound receivables will produce sound profits. We intend to continue to devote the necessary time and effort to see that our delinquencies and losses stay within acceptable limits.

Total retail receivables at September 30, 1966 were slightly in excess of $12,000,000, a new high. Unearned finance charges exceeded $2,000,000 and were 18.14% of retail receivables with precomputed interest. We are very pleased that we are able to show satisfactory

earnings while at the same time following conservative accounting policies which result in a high percentage of deferred income. Total unpaid balances of accounts with payments more than 60 days past due were 2.26% of total retail receivables at September 30, 1966. This is an increase of less than two-tenths of one percent during the past six months. At the same time the percentage of losses to retail receivables liquidated has decreased from 1.42% last year to 1.20% in the first six months this year. We are receiving increasing benefits from recoveries on previously written off accounts. Such recoveries were 12.60% of gross charge offs during the past six months, an increase over the 11.55% experienced last year.

During the past year a number of finance companies have deemed it advisable to change to a more conservative method of accounting which has required a significant increase in unearned finance charges with a corresponding reduction in earnings. In addition some companies have provided sizeable additional loss reserves which has also reduced their earnings. In our last annual report we described our accounting policies which, since they are already on the conservative side, will not have to be changed. In addition, although no one can predict future losses with absolute certainty, our delinquencies and loss experience lead us to believe that our reserve for losses is adequate to cover future losses on our present receivables.

You will notice that this report contains a complete set of audited financial statements and includes the report of our Chartered Accountants. As a part of the subordinated debt financing we completed last December, we agreed to have a complete audit twice a year. We believe this to also be a constructive move as far as our shareholders are concerned. You will know that your company is being independently audited twice a year. This also tends to strengthen the Company's position with its present and prospective lenders, especially in the U.S. market where having two audits a year has been standard practice for finance companies for quite some time.

Although we are not sure how soon it will be possible to acquire additional outside funds to support further growth, we are confident that we will eventually succeed. In the meantime your company is in strong financial condition and should be able to weather the present unsettled conditions without experiencing anything more damaging than a temporary leveling of a historical pattern of growth.

On behalf of the Board of Directors

President

FRONTIER ACCEPTANCE CORPORATION LIMITED
AND ITS WHOLLY OWNED SUBSIDIARIES

Consolidated Balance Sheet — September 30, 1966
(with comparative figures for September 30, 1965)

ASSETS

	1966	1965
Cash	$ 47,930	$ 19,697
Notes receivable:		
Retail (Note 1)	$12,015,954	$10,791,221
Wholesale	545,749	790,351
	$12,561,703	$11,581,572
Less:		
Unearned finance charges	$ 2,019,292	$ 1,791,803
Allowance for possible losses	137,048	110,701
	$ 2,156,340	$ 1,902,504
NOTES RECEIVABLE — NET	$10,405,363	$ 9,679,068
Accounts receivable	70,592	34,656
Prepaid expenses	8,081	9,124
Furniture, equipment and leasehold improvements — at cost	$ 34,613	$ 28,320
Less accumulated depreciation and amortization	16,580	11,499
	$ 18,033	$ 16,821
Unamortized debt discount and expense (Note 2)	148,467	30,632
	$10,698,466	$ 9,789,998

Approved on behalf of the Board:

L. W. OEHRING, JR., Director.

J. W. ADAMS, Director.

LIABILITIES AND SHAREHOLDERS' EQUITY

		1966	1965
Short-term notes payable — secured by assignment of certain notes receivable:			
Banks		$ 5,813,003	$ 6,617,265
Other			650,000
		$ 5,813,003	$ 7,267,265
Accounts payable and accrued liabilities		144,732	98,556
Income and other taxes payable		37,372	37,117
Dealers' credit balances		373,403	274,960
Preference dividend payable			7,885
Capital funds:			
Subordinated debt (Note 3):			
$6\frac{7}{8}$% Senior Subordinated Notes		$ 2,151,250	
$6\frac{3}{4}$% Subordinated Sinking Fund Debentures Series A		900,000	$ 937,000
TOTAL SUBORDINATED DEBT		$ 3,051,250	$ 937,000
Shareholders' equity:			
Capital Stock (Note 4):			
Authorized:			
35,370 first preference shares with a par value of $25 each, issuable in series	$884,250		
1,000,000 common shares without par value	—		
Issued:			
15,370 $6\frac{1}{2}$% cumulative redeemable convertible first preference shares Series A, with a par value of $25 each		$ 384,250	$ 475,000
188,685 common shares — stated value		512,963	432,213
		$ 897,213	$ 907,213
Retained earnings (Note 5)		381,493	250,002
Purchase fund — in respect of $6\frac{1}{2}$% cumulative redeemable convertible first preference shares Series A			10,000
TOTAL SHAREHOLDERS' EQUITY		$ 1,278,706	$ 1,167,215
TOTAL CAPITAL FUNDS		$ 4,329,956	$ 2,104,215
		$10,698,466	$ 9,789,998

See accompanying notes to financial statements

Subject to the accompanying report of Peat, Marwick, Mitchell & Co., Chartered Accountants, dated November 7, 1966

FRONTIER ACCEPTANCE CORPORATION LIMITED

AND ITS WHOLLY OWNED SUBSIDIARIES

Consolidated Statement of Earnings and Retained Earnings
Six Months Ended September 30, 1966

(with comparative figures for the six months ended September 30, 1965)

	1966	1965
Income — finance charges, interest and fees earned	$ 662,937	$ 571,047
Deduct:		
Salaries and wages	$ 85,410	$ 70,699
Other general and administrative expenses (Note 6)	103,985	71,622
Provision for possible losses	53,740	67,513
	$ 243,135	$ 209,834
EARNINGS BEFORE COST OF BORROWINGS AND TAXES ON INCOME	$ 419,802	$ 361,213
Cost of borrowings, principally interest (Note 2)	297,931	241,980
EARNINGS BEFORE TAXES ON INCOME	$ 121,871	$ 119,233
Taxes on income	58,000	56,926
NET EARNINGS	$ 63,871	$ 62,307
Retained earnings at beginning of period	329,918	210,780
	$ 393,789	$ 273,087
Deduct dividends on 6½% cumulative redeemable convertible first preference shares Series A	12,296	23,085
Retained earnings at end of period	$ 381,493	$ 250,002

See accompanying notes to financial statements

Subject to the accompanying report of Peat, Marwick, Mitchell & Co., Chartered Accountants, dated November 7, 1966

ACCOUNTANTS' REPORT

The Board of Directors
Frontier Acceptance Corporation Limited

We have examined the consolidated balance sheet of Frontier Acceptance Corporation Limited and its wholly owned subsidiaries as of September 30, 1966 and the consolidated statement of earnings and retained earnings for the six months ended on that date. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated balance sheet and consolidated statement of earnings and retained earnings present fairly the financial position of the companies at September 30, 1966 and the results of their operations for the six months ended on that date, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

The figures as at September 30, 1965 and for the six months ended on that date relating to the consolidated balance sheet and consolidated statement of earnings and retained earnings are provided for comparative purposes. As we did not carry out an examination of the companies as of September 30, 1965, we are not in a position to express an opinion of these figures.

Toronto, Ontario,
November 7, 1966.

PEAT, MARWICK, MITCHELL & CO.,
Chartered Accountants.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
Six Months Ended September 30, 1966

NOTE 1 — **Retail Notes Receivable**

Of the retail notes receivable outstanding at September 30, 1966, instalments aggregating \$3,833,274 are due within one year.

NOTE 2 — **Unamortized Debt Discount and Expense**

Unamortized debt discount and expense is shown net of accumulated tax reductions of \$35,766 and accumulated amortization of \$31,507. Of the latter amount, \$13,621 is applicable to the six months ended September 30, 1966.

NOTE 3 — **Subordinated Debt**

The 6⅞% Senior Subordinated Notes are payable, both as to principal and interest, in U.S. funds. The Notes are for \$2,000,000 (U.S.) and are shown at the rate of exchange on December 16, 1965, the date of issuance. The Notes are due December 15, 1977 and the Company has covenanted to establish a sinking fund to provide for the retirement of \$200,000 (U.S.) principal amount of the Notes on December 15, in each of the years 1968 to 1976, both inclusive. The Notes are presently redeemable, otherwise than out of sinking fund monies, in whole or in part at a premium of 5% of such principal amount if redeemed on or before December 15, 1966 with the premium thereafter decreasing ratably each year to zero if redeemed after December 16, 1976.

The 6¾% Subordinated Sinking Fund Debentures Series A are due June 15, 1979. The Company has covenanted to establish a sinking fund to provide for the retirement of \$50,000 principal amount of the Debentures on June 15, in each of the years 1965 to 1974, both inclusive, and \$100,000 principal amout of the Debentures on June 15, in each of the years 1975 to 1978, both inclusive. The Debentures are presently redeemable, otherwise than out of sinking fund monies, in whole or in part at a premium of 4.25% of such principal amount if redeemed on or before June 15, 1967 with the premium thereafter decreasing ratably each year to zero if redeemed after June 15, 1978.

NOTE 4 — **Capital Stock**

The 6½% cumulative redeemable convertible first preference shares Series A are convertible, on or before October 31, 1970, into common shares at the rate of 4 common shares for each first preference share Series A on or before October 31, 1967 and thereafter at a declining rate. The first preference shares Series A are redeemable at a price of \$26.00 a share. The Company is required to enter on its books to the credit of a purchase fund certain amounts to be used for the purchase of first preference shares Series A, which obligation can be anticipated by the redemption or conversion of first preference shares Series A. At September 30, 1966 no amounts were required to be set aside for such purchase fund.

Of the authorized and unissued common shares, 61,480 shares are reserved for conversion of the first preference shares Series A; 14,865 shares are reserved for share purchase warrants (issued in connection with the 6¾% Subordinated Sinking Fund Debentures Series A) exercisable at \$8.50 a share on or before June 15, 1967 and increasing to \$12.50 per share on or before expiration date June 15, 1970; 40,000 shares are reserved for share purchase warrants (issued in connection with the 6⅞% Senior Subordinated Notes) exercisable at \$6.25 a share on or before expiration date December 15, 1977; and 14,900 shares are reserved for executive stock options (issued to three officers) exercisable at \$6.25 a share. One option is for 10,000 shares exercisable at the rate of 2,000 shares per year and expires on February 28, 1975; one option is for 3,500 shares exercisable at the rate of 500 shares per year and expires on September 14, 1971; and one option is for 1,400 shares exercisable at the rate of 200 shares a year and expires on June 30, 1972. All options may be exercised on a cumulative basis.

NOTE 5 — **Retained Earnings**

The Company's various loan agreements and its Letters Patent relating to the first preference shares Series A contain provisions relating to the payment of dividends on common shares. Under the most restrictive of these provisions no amount of retained earnings was available at September 30, 1966 for the payment of dividends on common shares.

NOTE 6 — **Directors' Fees and Depreciation and Amortization**

Other general and administrative expenses includes directors' fees for services as such of \$2,100 (1965 — \$1,400) and depreciation and amortization of \$2,042 (1965 — \$2,112).

Frontier Acceptance Corporation Limited

DIRECTORS:	JOHN W. ADAMS C. NORMAN CHAPMAN MURRAY J. HOWE CHARLES E. ISARD PETER J. IVEY LYMAN W. OEHRING, JR. FRANK T. SHERK DAVID B. WELDON
OFFICERS:	LYMAN W. OEHRING, JR. — President C. NORMAN CHAPMAN — Vice-President HOWARD L. KIRBY — Vice-President JOHN A. PARK — Vice-President ROBERT W. STEVENS — Secretary PETER J. IVEY — Assistant Secretary
LEGAL COUNSEL:	BLAKE, CASSELS & GRAYDON, Toronto, Ontario
AUDITORS:	PEAT, MARWICK, MITCHELL & CO., Toronto, Ontario
BANKERS:	BANK OF MONTREAL, Toronto, Ontario THE ROYAL BANK OF CANADA, Toronto, Ontario
TRANSFER AGENT:	THE ROYAL TRUST COMPANY, Toronto, Ontario
SECURITIES LISTED:	TORONTO STOCK EXCHANGE 6½% cumulative redeemable convertible first preference shares Series A Common shares
TRUSTEE:	MONTREAL TRUST COMPANY, Toronto, Ontario 6¾% Subordinated Sinking Fund Debentures Series A
HEAD OFFICE:	5385 YONGE STREET, Willowdale (Metropolitan Toronto), Ontario
BRANCHES:	5385 YONGE STREET, Willowdale, Ontario 1111 MAIN STREET, Moncton, New Brunswick 110 PLACE CREMAZIE WEST, Montreal, Quebec